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COUNCIL BLUFFS GAS COMPANY

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COUNCIL BLUFFS GAS COMPANY

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April 26, 1955

COUNCIL BLUFFS GAS COMPANY

HISTORY

Council Bluffs Gas Company was incorporated in Delaware on April 14, 1928, as a wholly-owned subsidiary of Union Utilities, Inc., a holding company which was also organized in Delaware, on March 22, 1928, for the purpose of acquiring a number of gas properties, principally in Texas. Shortly after its formation, Council Bluffs Gas acquired all of the gas properties in Council Bluffs and immediate vicinity then owned and operated by Citizens Gas & Electric Company of Council Bluffs which had been incorporated in New Jersey on November 13, 1900. This latter company was a wholly-owned subsidiary of Nebraska Power Company, into which it was subsequently merged. Nebraska Power, of course, was liquidated after formation of the Nebraska Public Power System, and its electric properties in Council Bluffs have since passed into the hands of Iowa Power and Light Company.

Ownership of Council Bluffs Gas was acquired by Lone Star Gas Company on September 30, 1929 when that company purchased all of the principal gas properties then owned by Union Utilities, Inc. In 1942 Lone Star Gas was ordered by the SEC, pursuant to requirements of the Holding Company Act, to divest itself of Council Bluffs Gas Company. In accordance therewith, all of the outstanding securities of Council Bluffs Gas Company were sold by Lone Star to Raymond A. Smith of Council Bluffs, acting as nominee. The Common stock, we understand, is held by a small group of individuals.

The conversion to natural gas was undertaken by Lone Star Gas and during its ownership of the properties over $1,000,000 was expended in rehabilitating the property and for additions and betterments, and, as would be expected, under Lone Star management excellent construction standards were employed and the system was put in first class operating condition.

BUSINESS AND TERRITORY

The Company is engaged in natural gas distribution operations in Council Bluffs, Iowa, and its immediate vicinity, and for promotion purposes also sells gas appliances. Revenues from gas sales were $2,713,903 for the 12 months ended December 31, 1954, and were divided approximately 61% residential, 9.6% commercial, and 29.4% industrial. Prior to 1954 industrial revenues accounted for a much smaller percentage of total revenues (11.5% in 1953). During

1954, however, Iowa Power & Light Company completed a 44,000 kw. modern, efficient steam plant near the city limits of Council Bluffs, and this plant consumed a relatively large amount of gas, although it was not in operation for the full year. Total sales volume in M.c.f. amounted, in 1954, to 5,069,823 and 14,065 customers were served at the end of 1954. We are giving below data with regard to M.c.f. sales, revenues, and the average number of customers served by years during the period 1945-1954 and as percentages of 1945:

	MCF		Revenue		Avge. Number of Customers	
	Amount	% of 1945	Amount	% of 1945	Amount	% of 1945
1954	5,069,823	359	$2,713,903	369	13,783	140
1953	2,952,250	209	1,922,467	261	13,330	135
1952	3,012,402	213	1,781,571	242	12,868	130
1951	3,063,018	217	1,723,321	234	12,377	125
1950	2,744,836	195	1,416,734	193	11,827	120
1949	2,260,309	160	1,182,288	161	11,246	114
1948	1,975,409	140	1,045,644	142	10,892	110
1947	1,896,919	134	1,010,178	137	10,564	107
1946	1,523,417	108	818,275	111	10,189	103
1945	1,410,995	100	735,837	100	9,864	100

On an annual basis the increase in the number of customers served has been of rather modest proportions but during the nine year period the increase in average number of customers served was 40%. During the same period the increase in revenues was 269% and the increase in M.c.f. output was 259%. The increase in Mcf. sales and in revenues was unusually large in 1954, amounting to about 72% in M.c.f. and 37% in revenues, which was due in part to rate increases and in part to very substantial sales of gas made to Iowa Power & Light Company. Prior to 1954, however, the increase in M.c.f. sales and revenues was excellent and amounted to 109% for M.c.f. sales and 161% for revenues between 1945 and 1953.

Council Bluffs, the seventh largest city in Iowa with a 1950 population of 45,429, is located on the extreme western boundary of the state along the Missouri River, directly across from Omaha, Nebraska. It is primarily a railroad center, and also has miscellaneous, but relatively small, manufacturing industries. In addition, it serves as the focal point for a surrounding eight-county agricultural area. The city has been largely unaffected by war and defense industries over the last decade or more, but has experienced a fair degree of economic and population expansion. Population statistics covering 1930-1940 and 1940-1950 for Council Bluffs, as well as for the township (Kane) and county (Pottawattamie) within which it lies, are shown in the following table:

	Population			% Increase	
	1950	1940	1930	1940-50	1930-40
Council Bluffs	45,429	41,439	42,048	9.6	1.4*
Kane Township	46,929	42,590	43,040	10.2	1.0*
Pottawattamie County	69,682	66,756	69,888	4.4	4.5*

* Indicates Decrease.

Between 1930 and 1940 the population of Council Bluffs declined 1.4%, which was in line with the experience of Kane Township, which had a population decrease of 1.0% at that time. The 1930-1940 loss of residents was not essentially due to any population shift to outlying suburban areas as indicated by the 4.5% loss for all of Pottawattamie County. During 1940-1950 population growth for Council Bluffs and Kane Township was 9.6% and 10.2% respectively, which largely reflected urban development and an influx of former rural residents. In that period, the population gain for Pottawattamie County was only 4.4%. Continuing but moderate expansion in Council Bluffs is indicated by an estimated 2.4% population increase from 1950 to 1955, whereas Pottawattamie County showed a 0.3% decline in that time.

A conditioning factor with respect to the comparatively moderate population gain in Council Bluffs is the city's secondary position relative to adjacent Omaha with a 1950 population of 251,117. General business activity in Omaha, with a wide range and large number of commercial establishments and a fairly high proportion of manufacturing industries, is comparatively much more diverse and intensified than in Council Bluffs. This, in turn, has been conducive to reasonably satisfactory growth as indicated by a 12.7% population gain for the Omaha Metropolitan Area between 1940 and 1950. The metropolitan area, incidentally, lies principally in Nebraska but also includes Kane and several other townships on the east side of the Missouri River in Iowa. Population increases for Iowa and Nebraska were 3.3% and 0.7%, respectively from 1940 to 1950, while for the nation the gain was 14.5%.

The importance of Council Bluffs as a railroad and trading center, its principal facets of economic support, is brought out by the following employment statistics for the city as taken from the 1950 Census.

	Total Employed	% of Total
Agriculture, Forestry, etc.	266	1.5%
Construction and Mining	939	5.3
Manufacturing:		
Durables	997	5.6
Nondurables	1,191	6.6
Transportation and Public Utilities	4,740	26.6
Wholesale and Retail Trade	4,490	25.1
Finance, Insurance and Real Estate	944	5.3
Business and Personal Services	3,293	18.5
Public Administration and Other	975	5.5
Total Employed	17,835	100.0%

Of the city's 17,835 employed residents at 1950, an unusually high 26.6%, in the amount of 4,740, were in the transportation and public utility employment category. Within that classification, employment by railroads and railway express service comprised almost 72% with the balance accounted for by trucking services, other transportation, and other utilities. The significance to the Council Bluff's economy of such a very high proportion of employment in transportation and other public utilities is emphasized by a comparison with Chicago, the nation's leading rail center, which at 1950 had only about 10% of those employed within that category. Council Bluffs is served by seven railroads: Burlington-Great Western, Northwestern, Illinois Central, Rock Island, Union Pacific, Milwaukee, and the Wabash. A number of these roads maintain repair shops in the city and there are, of course, other facilities for the handling of cargoes such as a large railway mail exchange terminal, and the maintenance of equipment. Council Bluffs is the eastern terminus of the Union Pacific whose trains continuing east are switched over to the Chicago & North Western at that point.

The second most predominant employment classification, wholesale and retail trade, accounted for 4,490 persons, or 25.1% of the total, in 1950, which indicates the position of Council Bluffs as a distribution center for surrounding farm areas, even though a substantial portion of the city's residents commute to Omaha where commercial trading activity is much larger. One factor, as far as trading areas are concerned, is that Nebraska has no sales tax while there is a 2% state sales tax in Iowa, which tends to result in the population of Council Bluffs doing less trading within the city than otherwise would be the case.

Manufacturing employment in Council Bluffs is about evenly apportioned between durables and nondurables, but it is apparent that such employment, at only 12.2% of the 1950 total, is not too important to the city's economy. Here again, Council Bluffs occupies very much of a secondary position to Omaha where, in 1950, manufacturing in relation to total employment was 20.5%. This latter proportion, however, is still relatively low by comparison with many other urban centers in the nation, a reflection of substantial dependence of the Omaha metropolitan area on the processing and distribution of agricultural produce from an extensive, surrounding farming region.

Among the larger manufacturing employers in Council Bluffs are: Blue Star Produce - poultry processors (350); Griffin Wheel Co. - railroad wheels (300); Giant Manufacturing Co. - truck bodies and playground equipment (300); Omaha Standard Body Co. - truck bodies (300); and Howard Manufacturing Co. - plastic bags (100). From the standpoint of industrial sales rather than employment, much the most important customer in 1954 was Iowa Power & Light Company which accounted for about 36.5% of M.c.f. sales. Such sales, however, were made on an interruptible basis at a relatively low profit margin. The second most important customer is the Union Pacific Railroad which consumed 172,887 M.c.f. in 1954, equivalent to about 3.4% of total M.c.f. sales, and the second most important group of industrial customers were greenhouses which consumed 191,289 M.c.f., or about 3.75% of M.c.f. sales. Other relatively important industrial customers were the Iowa School for the Deaf, school districts, and hospitals.

Business and personal services also account for a fairly high proportion of employment in Council Bluffs (18.5% at 1950) and again this probably reflects a sizable proportion of Council Bluffs' residents in that category who commute to Omaha. The remainder of the employment classifications included in the table on page 4 are not of sizable proportions and require no further comment for present purposes.

As the tabulation on page 2 indicates, the Company's growth in business has been steady and consistent even prior to 1954 when the large Iowa Power & Light load was obtained, notwithstanding the comparatively moderate population growth in the service area. The cost of gas sold by the Company enjoys a price differential in comparison with both coal and fuel oil, and this has lead to comparatively high space heating saturation estimated by the Company at about 95%. The degree day deficiency is about 6,100 for the territory, which, of course, has also been an important contributing factor to the development of the heating load, and the Company has been very aggressive in merchandising appliances.

All factors considered, we believe that the territory served by the Company is attractive for the distribution of natural gas, although we would not expect a rapid increase in population or a rapid increase in use per domestic customer in view of the high saturation of house heating business. At the end of 1954 the Company was serving approximately 85 customers per mile of transmission and distribution main, which is a good density for a system of this kind, particularly when tied up with revenue per domestic customer which approximated $129 in 1954.

If the Company continues to sell gas on an interruptible basis to Iowa Power & Light for boiler fuel, M.c.f. sales and revenues from this source are likely to increase over 1954 levels, partly because the plant of that company was on the line for only a portion of the year and partly because there is a possibility that a second unit of 66,000 kw. capacity will be built by Iowa Power & Light at its Council Bluffs station in 1958 or 1959. Iowa Power & Light, however, is now experimenting with Oklahoma coal for boiler fuel and this situation will be discussed later in our report.

PROPERTY

The principal physical properties owned by the Company consist of transmission and distribution facilities. Prior to 1952 the Company owned a small gas manufacturing plant capable of producing about 2,000,000 cubic feet of 1,000 B.t.u. gas per day, but the gas manufacturing equipment was retired from service in 1952 because of obsolescence and the Company installed propane-air equipment to provide for peak shaving gas. The building containing the manufactured gas facilities has been maintained, and one boiler in the plant is maintained for furnishing heat to the gas holders in winter months. The propane-air equipment consists of storage capacity of twelve 30,000 gallon tanks and vaporizing equipment capable of producing 7,500 M.c.f. equivalent of 1,000 B.t.u. gas. In addition the Company owns and maintains two small gas holders, one of 500,000 cubic feet and the other of 200,000 cubic feet capacity. The Company also maintains compressor equipment which is used to inject this propane-air gas into its intermediate high pressure system.

We are giving at the top of the following page a tabulation which shows the transmission and distribution system as of December 31, 1954 by sizes and types of pipe:

Size of Main	Length of Main		
	Cast Iron	Steel	Total
1-1/4		5,456 ft.	5,456 ft.
1-1/2		3,306	3,306
2		171,212	171,212
2-1/2		621	621
3		3,659	3,659
4	359,084 ft.	74,646	322,730
6	112,062	9,813	121,875
8	38,718	32,029	70,747
12	11,000	21,150	32,150
16		29,700	29,700
Total	520,864	351,592	872,456
13,912 Service Lines			703,348 ft.

When Lone Star acquired the property many years ago the distribution system was entirely cast iron and most of the service connections were so-called "black pipe" with no protective covering. Lone Star constructed a secondary intermediate pressure system to feed a number of district regulators which in turn were connected to the low pressure cast iron system. A large number of old services were replaced with wrapped steel pipe, the minimum diameter of which has been standardized at 1-1/4 inches, and it will be noted that most of the distribution system now consists of 2-inch, 4-inch, and 6-inch mains.

The main line of Northern Natural Gas Company, from which Council Bluffs Gas obtains its entire supply of gas, passes about 18 miles south of Council Bluffs. The interconnection with the Company is made from a tap on the east side of the Missouri River running north to a point about five miles south of the city where Northern maintains a pressure regulating and dehydrating station. From this point on, however, ownership of the 16-inch line into Council Bluffs rests with the Company. The 16-inch line extends into the Company's own pressure regulator station located at the site of the old manufactured gas plant, which structure is still in existence. Gas is received from Northern at a pressure of approximately 45 to 50 pounds and is reduced at the Company's own regulating station to 25 pounds for intermediate distribution to the district regulating stations. At one time Northern itself owned a line from the regulating station northwest across Council Bluffs for the purpose of serving several industrial plants of the Omaha Public Power District. As a result of this abandonment of service by Northern and the removal of its 8-inch line, Council Bluffs Gas no longer has an interconnection for an additional source of supply which this line at one time afforded. However, the Company and the

Metropolitan Utilities District of Omaha are negotiating with Northern Natural Gas to jointly acquire a line which is carried across the river by the bridge connecting Omaha and Council Bluffs with the intention of using it in the case of emergency transportation of gas in either direction between the two cities.

The Company now operates 13 district regulating stations plus 21 pit regulators for relatively small areas. The intermediate pressure system which loops the city operates at about 25 pounds and the low pressure system at 4-ounce pressure. The dual pressure system has permitted the serving of relatively large use industrial customers directly from intermediate pressure lines, thus avoiding heavy volume demands on the low pressure system. The Company oil fogs all gas passed through the regulator stations.

The system appears to be very tight and on the average there has been a negative leakage loss which has been due to the fact that purchases are based on an 8-ounce gas pressure whereas sales are made at a 4-ounce pressure. Correction for the pressure difference, however, would still result in a very low leakage loss.

In 1954 the Company completed an 8-inch transmission main from the border station of Northern Natural Gas to the power plant of Iowa Power & Light Company, a distance of 2.8 miles. This line has been constructed to carry line pressures of 300 pounds in cold weather and 250 pounds in the summer. This line is also tied into the 16-inch transmission line of the Company to afford emergency service.

In 1948 the Company constructed an office building at a cost, exclusive of land and equipment, of approximately $110,000. Other property owned by the Company consists of transportation equipment and miscellaneous equipment, including storage facilities and facilities for meter testing.

The system was virtually rebuilt after it was acquired by Lone Star Gas and about one-third of the present investment in plant has been added in the last 10 years. The physical property of the Company has been well designed and maintained, and is of adequate size to afford excellent service. As previously mentioned, there has been a negative leakage loss on balance for a number of years.

<u>Natural Gas Supply</u>: The Company purchases gas from Northern Natural Gas Company, which is one of the older and better known gas transmission systems in the United States. At the end of 1954 proven reserves controlled by Northern at the source of supply were estimated by that company at 9.0 trillion cubic feet, and of this amount 5.2 trillion cubic feet are controlled by gas purchase contracts between Northern and independent producers, 1.5 trillion are controlled by gas purchase contracts

with Northern Natural Gas Producing Company, and 2.3 trillion are controlled by gas purchase contracts between the Permian Basin Pipeline Company, a subsidiary of Northern, and independent producers. Gas sales by Northern in 1954 amounted to 273 billion cubic feet and the estimated proven reserves were equivalent to a 33-year supply based on 1954 sales. Over a period of years the total estimated gas reserves of Northern have on balance been increasing, and the 9.0 trillion cubic feet figure at the end of 1954 compares with approximately 4.3 trillion at the end of 1948.

Northern Natural Gas has entered into an agreement for the purchase of gas from Trans-Canada Pipe Lines, Ltd., and if FPC approval is obtained Northern estimates that the importation of natural gas from Canada into Northern's system can add 1.3 trillion cubic feet of Canadian gas to Northern's reserves. The importation of gas, however, is being opposed by a number of utility companies, including Council Bluffs Gas Company, because of the belief that the purchase of gas from Canada would increase the over-all cost of gas to Northern's customers substantially. We understand that it now appears that the Trans-Canada Pipe Line project will be delayed to a point where Northern will not be able to obtain any Canadian gas before 1956, even if FPC approval is obtained.

Also of importance in considering the supply of gas to Northern's customers are developments being made by Northern in connection with their storage project located west of Des Moines. While this storage will not be developed for really effective use before the 1956-1957 heating season, it is a substantial project and one which could develop to be very large, with the ultimate storage capacity being in the neighborhood of 50 billion M.c.f. There are two structures in the storage area and the deeper structure is apparently going to work out to be the better one. It is estimated that during the 1956-1957 heating season the storage capacity could provide up to 200,000 M.c.f. of daily deliverability capacity. The present expansion and construction program of Northern is now before the FPC for certification, including the proposal to purchase Canadian gas, but no decision has yet been rendered by that Commission.

VALUATION

In the following short tabulation we show the December 31, 1954 balance sheet of Council Bluffs Gas in condensed form:

Assets:	
Utility Plant	$3,764,246
Less: Reserve for Depreciation	1,262,749
Contributions for Construction	19,834
Net Utility Plant	2,481,663
Sinking Fund - 5% Preferred Stock	31,631
Current and Accrued Assets	393,042
Deferred Debits	11,374
Total Assets	3,117,710

(Continued)

(continued)

Liabilities:	
Mortgage Bonds	$ 880,000
Notes	240,000
Preferred Stock	504,000
Common Stock and Surplus	706,206
Total Capitalization	2,330,206
Current and Accrued Liabilities	783,502
Deferred Credits	4,002
Total Liabilities	3,117,710

For the purposes of this study we have included in current and accrued assets $8,966 of prepaid insurance which, in the audit report, has been included as a deferred debit. We have also eliminated from current liabilities the sinking fund payment due September 1, 1955 on the First Mortgage Bonds, as well as the May 15, 1955 payment due on Long-Term Notes Payable.

Utility Plant: The table below shows the Utility Plant account in detail at the balance sheet date:

	Amount		% of Total
Intangible Plant:			
Organization	$ 7,053	$	
Franchises	9,048	16,101	0.4
Production Plant:			
Manufactured Gas Equipment	146,574		
Propane Equipment	224,199	370,773	9.8
Distribution Plant:			
Land	56,368		
Right of Way	986		
Structures and Improvements	101,617		
Mains	1,540,867		
Measuring & Regulating Equipt.	47,225		
Services	576,786		
Meters	261,606		
Meter Installations	44,689		
House Regulators	12,712		
House Regulator Installations	10,776		
Other Distribution System Equipt.	39,654	2,693,286	71.5
General Plant			
Land	6,334		
Structures and Improvements	110,095		
Office Furniture & Equipment	34,922		
Transportation Equipment	46,831		
Tools & Work Equipment	24,033		
Miscellaneous General Plant	3,699	225,914	6.0
Utility Plant in Service		3,306,074	87.7
Other Tangible Property		453,677	12.2
Construction Work in Progress		4,537	0.1
Utility Plant		3,764,288	100.0
Less: Reserve for Depreciation		1,262,791	
Contributions for Constr.		19,834	
Net Utility Plant		2,481,663	

A breakdown of utility plant was taken from the Company's December operating report as the audit does not give such a breakdown. The difference between total utility plant per audit and per the December operating report, however, was only $42.00.

So far as we know there has never been an original cost study made of the properties of Council Bluffs Gas Company. As of June 1, 1928 an appraisal was made by William E. Barrett, Engineer, of cost of reproduction new less accrued depreciation of the property, and this appraisal indicated a value at that time of $1,858,472.01. The cost to Union Utilities of its investment in the Company at the same time apparently was $1,697,227.01, which was $161,240 less than the Barrett cost of reproduction new less accrued depreciation of the properties. The difference of $161,245 was set up by Union Utilities as capital surplus. This figure, however, as we understand it, was not necessarily the difference between the carrying value on the books of the predecessor company and the cost of reproduction new less accrued depreciation valuation, but was simply the difference between such cost of reproduction figure and the cost to Union Utilities.

In December 1931 Lone Star Gas Corporation made an entry to reclassify and adjust Investment Accounts which resulted in a credit to Gas Manufacturing Investment and a debit to Other Undistributed Fixed Capital of $449,674.87, and a charge to Other Undistributed Fixed Capital of $12,500 and a credit to Intercompany Accounts Payable - Lone Star Gas Corporation for a similar amount.

In March 1932, $152,747 was transferred from Miscellaneous Construction Costs, which were carried in the Plant Property Investment Account, to Other Undistributed Fixed Capital. In November 1938 the credit balance of $161,245 in Capital Surplus which existed as a result of the Barrett appraisal was transferred to Undistributed Fixed Capital Account, which reduced it to $453,676.87. When a new classification of accounts became effective in 1940 the title of Undistributed Fixed Capital Account was changed to Other Tangible Property--General, where it still exists in the amount of $453,676.87. The Company has not reduced this amount through amortization and, we understand, has not been able to substantiate this figure as representing Depreciable Tangible Property for income tax purposes. The account Other Tangible Property therefore appears to us to be a write-up which, however, may or may not be the difference between actual original cost and present total carrying value of utility plant. Some portion of this figure, however, might be included in a rate base, and if an original cost study were made it is entirely possible that such a figure would exceed the present carrying value of Utility Plant in Service which amounted to $3,306,074 as of December 31, 1954. For the purpose of this report, however, we believe that Other Tangible Property in the amount of $453,677 should be eliminated from the total carrying value of Utility Plant in arriving at a "bare bones" valuation.

At the time we prepared our 1944 report on Council Bluffs Gas Company we made a detailed study of the utility plant account and we also reviewed the property base allowed for Federal income tax purposes. As of December 31, 1944 our estimate of the undepreciated value of utility plant was $2,192,000 and our estimate of depreciated value was $1,450,000. Both of these estimates were well below the book figure because we reduced the value of manufactured gas equipment and eliminated the Other Tangible Property account. In 1952 the Company retired approximately $235,000 of manufactured gas equipment, bringing this segment of plant down to what we would consider to be a reasonable figure.

The depreciation reserve at the end of 1954 amounted to $1,262,791, a figure equivalent to 39.1% of depreciable plant, which appears to us to represent an entirely adequate figure. While 75% of the gross book value of utility plant in service has been added since Lone Star Gas took over many years ago, a substantial portion of the present properties is relatively old and gross additions have not been nearly as large during the postwar period as has been the case for many utility properties.

All factors considered, it seems to us that the net book value of Utility Plant in Service, plus construction work in progress which aggregated $2,028,000 as of December 31, 1954, would represent a minimum value and can be used for the purpose of this report. We recognize that there is no state commission in Iowa with regulatory powers over the Company, and we also recognize that for rate-making purposes a considerably higher figure might be established. The gross book value of utility plant in service plus construction work in progress, which aggregated $3,310,611 as of December 31, 1954, was equivalent to about $240 per customer and the net book value of utility plant in service plus construction work in progress was equivalent to only about $147 per customer. We believe that it would probably cost in the neighborhood of $300 to $350 per customer to reproduce the system today, which would indicate a reproduction cost new of between $4,100,000 and $4,800,000, and a reproduction cost new less depreciation (assuming a 39.1% depreciation reserve) of $2,500,000 to $2,900,000.

Other Assets: The year-end 1954 balance sheet showed $31,631 of investment and fund accounts, which amount consists entirely of sinking funds for the 5% Preferred stock. At the balance sheet date there was a net working capital deficit of $190,460, as is indicated by the tabulation on the following page showing a breakdown of current assets and current liabilities:

Current and Accrued Assets:	
Cash	$202,336
Accounts Receivable	306,211
Materials and Supplies, and Inventories of Appliances	75,529
Prepayments	8,966
Total Current and Accrued Assets	593,042
Current and Accrued Liabilities:	
Accounts Payable	214,240
Customers' Deposits	78,581
Accrued Taxes	452,152
Accrued Interest	38,529
Total Current and Accrued Liabilities	783,502
Net Working Capital Deficit	190,460

Normally, Council Bluffs Gas does not have a cash position of over $200,000 nor are accrued taxes as high as $452,000. These two accounts are distorted somewhat by the fact that Northern Natural, during 1954, made substantial refunds applicable to several rate increases made under bond over the past several years, and this served to build up the cash position and also to increase income tax liability.

Accounts Payable, which amounted to $214,240 at the end of 1954, are likewise comparatively high. This, however, is due to the fact that merchandise accounts receivable amounted to $100,249 and that Accounts Receivable from Iowa Power & Light Company and Union Pacific Railroad at year-end 1954 totaled $50,400. Past due balances either in connection with the sale of gas or the sale of appliances which were over 30 days' past due were very small, indicating an excellent collection record for the Company. Included in current liabilities were customers' deposits of $78,581 which are not, strictly speaking, a current liability.

As indicated, the Company had a net working capital deficit of approximately $189,000 at the balance sheet date, which is a rather sizable figure for a company of this type.

Summary: In the following short tabulation we have summarized our ideas of minimum values:

Net Utility Plant	$2,028,000
Investment and Fund Accounts	31,631
Net Working Capital Deficit	190,460*
Total	1,869,171

* Red figure.

CAPITALIZATION

We are giving below the capitalization and capitalization ratios of the Company as of December 31, 1954:

First Mortgage Bonds	$ 880,000	37.8%
Notes Payable	240,000	10.3
Total Long-Term Debt	1,120,000	48.1
Preferred Stock	504,000	21.6
Common Stock	320,000	13.7
Earned Surplus	384,050	16.5
Capital Surplus	2,156	0.1
Total Capitalization	2,330,206	100.0

It will be noted that the ratio of First Mortgage debt to total capitalization was 37.8% at the end of 1954, and that the ratio of long-term debt to total capitalization was 48.1%. Preferred stock outstanding at the end of 1954 was equivalent to 21.6% of total capitalization and Common stock equity was equivalent to 30.3%.

On January 1, 1955 the sinking fund on the Preferred stock which amounts to $31,500 annually, equivalent to 5% of the amount originally sold in 1950, became due and was paid, thus reducing the amount of Preferred stock to $472,500. Giving effect to the reduction (cash for which was included in the Sinking Fund Deposit) the Common stock equity would have been 30.8%.

As a matter of interest we are showing in summary form the capitalization and capitalization ratios of the Company as of December 31, 1954, December 31, 1950, and December 31, 1944:

	Amount 1954	% of Total	Amount 1950	% of Total	Amount 1944	Total
	$		$		$	
Long-Term Debt:						
First Mtge. Bonds	880,000	37.8	1,000,000	41.6	1,175,000	54.9
Notes Payable	240,000	10.3	250,000	10.4	-	-
Total Debt	1,120,000	48.1	1,250,000	52.0	1,175,000	54.9
5% Cumulative Preferred - $100 Par	504,000	21.6	630,000	26.2	-	-
Total Debt and Preferred	1,624,000	69.7	1,880,000	78.2	1,175,000	54.9
Common Stock Equity	706,206	30.3	524,257	21.8	965,346	45.1
Total Capitalization	2,330,206	100.0	2,404,257	100.0	2,140,346	100.0

There have been material changes in the Company's capitalization since it sold $1,175,000 of First Mortgage Bonds in 1944, although the total capitalization of the Company has increased only moderately since that time from $2,140,346 at the end of 1944 to $2,330,206 at the end of 1954.

At the end of 1944 the Company's capitalization was represented by First Mortgage debt and Common stock equity and the ratios were 54.9% and 45.1%, respectively. The Common stock equity, however, at the end of 1944 was made up of Common stock stated at $320,000, capital surplus of $632,156, and earned surplus of $13,190. In 1946 the capital surplus was reduced by $630,000 representing a stock dividend payable through the issuance of 6,300 shares of $100 par value Preferred stock. In 1950 the Articles of Incorporation were amended to create 6,300 shares of 5% Cumulative Preferred stock (exchanged for a like amount of 4% stock issued in 1946) which was sold to three institutions in 1950. This stock was sold by stockholders and not by the Company.

In 1945 the Company refunded the $1,125,000 of First Mortgage Bonds which were originally sold in the amount of $1,175,000, through the issuance and sale of $1,150,000 First Mortgage (closed) 3-1/4% Bonds due October 1, 1970.

Between the end of 1950 and the end of 1954 there has been a material improvement in the Company's capitalization and capitalization ratios. The amount of First Mortgage Bonds has been reduced from $1,000,000 to $880,000, total long-term debt was reduced from $1,250,000 to $1,120,000, the amount of 5% Preferred stock outstanding was reduced from $630,000 to $504,000, and Common stock equity increased from $524,257 at the end of 1950 to $706,206 at the end of 1954. As a result, the Common stock equity related to total book capitalization increased from 21.8% at the end of 1950 to 30.3% at the end of 1954.

First mortgage debt, which amounted to $1,175,000 at the end of 1944, was equivalent to about 81% of our then estimated minimum value of physical property, whereas the amount of First Mortgage Bonds now outstanding, $880,000, is equivalent to about 43.5% of our estimate of minimum value for physical property at the end of 1954.

Indenture Securing First
<u>Mortgage (closed) 3-1/4% Bonds</u>: As these Bonds are held by two insurance companies, only brief reference will be made to indenture terms. The most unusual feature of the indenture is that the issue was closed at $1,150,000, with the result that no additional First Mortgage Bonds can be issued. The indenture contains a sinking fund, requiring the payment of $30,000 annually on September 1 of each year commencing with the

year 1946, which is designed to retire $750,000, or 65%, of the original amount of First Mortgage Bonds by the maturity, October 1, 1970. The indenture contains a Renewal Fund which is not onerous. Under the Renewal Fund the Company agrees to charge and expend annually from income the greater of book depreciation appropriations, depreciation claimed for income tax purposes, or $30,000 plus an amount equal to 2% of the net depreciable property additions. The Company, however, may obtain as a credit against this fund, the amount of all expenditures made for property additions and the principal amount of Bonds retired through the sinking fund.

Under the indenture the Company agrees that it will not pay or declare any dividends on any shares of any class of its capital stock, or purchase, redeem or retire any shares of any class of capital stock unless, after giving effect to such action, the net income of the Company accrued subsequent to December 31, 1944, plus $7,000, shall be greater than total dividends declared or paid, plus any stock redeemed or retired over such amounts as shall have been received as the net cash proceeds of sales of shares of stock, subsequent to December 31, 1944. In effect, dividends are limited to net income less the amount of 5% Preferred stock being retired through the sinking fund. Based on the audit reports of the Company which will be discussed in more detail later, net income between December 31, 1944 and December 31, 1954 has totaled $1,473,551, and total dividend payments plus the retirement of Preferred stock during the same period have aggregated $1,304,517, thus leaving $169,034 of undistributed net income.

The First Mortgage Bonds are subject to redemption at various premiums and the redemption price which prevails from October 1, 1954 to October 1, 1955 is 102-3/8, with the redemption price declining 1/8 of 1% annually subsequent to that date. However, under the Loan Agreement referred to on page 17, the First Mortgage Bonds cannot be redeemed, except for sinking fund purposes, without the consent of the bank holding the major portion of Notes Payable.

Provisions With Respect to the <u>5% Cumulative Preferred Stock</u>: The Certificate of Incorporation of the Company was amended prior to the time when the present 5% Preferred stock was sold to three institutions. The total number of shares authorized and issuable is 6,300 shares of 5% Preferred stock and 13,500 shares of Common stock. There are a number of restrictive provisions in the Certificate of Incorporation as amended in 1950 which we are summarizing as follows:

1. The Company cannot reissue any shares of Preferred stock retired through the sinking fund which, as previously mentioned, amounts to $31,500 annually, or 5% of the initial issue.

2. Without the consent of the holders of 75% of the Preferred stock, no other class of stock can be created nor can the authorized Preferred stock be increased. In addition, no long-term indebtedness can be created or issued which would increase the ratio of funded debt to over 50% of total capitalization. This provision, of course, is very restrictive as far as future debt financing is concerned.

3. Dividends on the Common stock are limited to net income subsequent to December 31, 1949; no dividends can be paid which would result in an increase of the ratio of long-term debt to total capitalization to more than 50%; no dividends can be paid on the Common if the Common equity is less than 20%; dividends on Common stock are limited to 50% of amounts available for such dividends if the Common equity is less than 25% of total capitalization, and dividends are limited to 75% of the balance for Common if the Common equity is 30% or less. There is no limitation on the payment of Common dividends if the payment of such dividends does not reduce the Common equity below 30%.

4. If dividends on the Preferred stock are in arrears for one year or if the sinking fund on the Preferred is not paid, the Preferred can elect a majority of the Board of Directors. Otherwise the Preferred stock has no voting rights.

5. The redemption price of the Preferred stock is 105.

Provisions Covering
<u>Notes Payable to Banks</u>: In 1953 the Company discontinued its policy of short-term borrowing and entered into a loan agreement with the American National Bank and Trust Company of Chicago under which the Company could, under certain circumstances, borrow up to $500,000 to be payable in equal annual installments over a five-year period. Notes payable bear interest at 5%, but the Company has the right to prepay all or any part of the loans made under the bank agreement, at par. The Company borrowed $300,000 under this agreement.

While the maximum bank commitment was $500,000, this amount is reduced proportionately during the term of the agreement. Any part of the maximum amount which has not been taken by the Company at any maturity date shall be proportionately cancelled in the ratio that the amount of the loan maturing at such date bears to the unpaid balance of the borrowing. The maximum amount which the Company may borrow under this Agreement was reduced to $400,000 after the May 15, 1954 installment was paid, and will be reduced further as future installments are paid.

Sinking Fund Requirements: The present sinking fund requirements, including the $60,000 serial payment on Notes Payable, are comparatively heavy, aggregating as they do $121,500 annually, made up of $30,000 on First Mortgage Bonds, $60,000 on Notes Payable, and $31,500 on Preferred stock. Such annual payments are equivalent to approximately 7-1/2% of the total amount of Mortgage Bonds, Notes Payable, and Preferred stock outstanding at the end of 1954.

EARNINGS

We are giving on the following page income accounts of the Company for the years ended December 31, 1950-1954, which have been reproduced from the annual audits certified by Haskins & Sells.

As a matter of interest also we are giving below a tabulation which shows the trend in operating revenues, gross income, and net income for the years 1946-1954 which likewise have been taken from the Haskins & Sells audit:

	Operating Revenue	% of 1946	Gross Income	% of 1946	Net Income	% of 1946
1954	$2,714,904	332	$290,712	164	$240,153	268
1953	1,922,467	235	186,229	105	133,630	149
1952	1,781,571	218	258,703	146	130,011	145
1951	1,723,321	211	223,313	126	174,036	194
1950	1,416,734	173	249,052	141	201,510	224
1949	1,182,288	144	220,245	124	177,897	198
1948	1,045,644	128	197,708	112	144,012	160
1947	1,010,178	123	181,734	103	132,182	147
1946	818,275	100	176,992	100	89,838	100

The earnings of the Company for a number of years have been distorted, in our opinion, by the four wholesale gas rate increases made, under bond, by Northern Natural Gas Company which covered a portion of the year 1950 and the years 1951-1954 inclusive. With the exception of Northern's rate increase in the last quarter of 1950, which the Company deferred and which amounted to $19,271 before taxes, the Company has absorbed the higher cost of gas in its reported earnings, although a portion of such increased cost was passed along in the form of a rate increase to its customers made late in 1953. Because of the fact that the rates filed by Northern Natural Gas Company were reduced as the result of orders of the

	1954	1953	1952	1951	1950
	$	$	$	$	$
Operating Rev. from Natural Gas Sales	2,713,903	1,922,467	1,781,571	1,723,321	1,416,734
Operating Rev. Deductions:					
Operation	1,937,463	1,342,874	1,163,217	1,088,471	867,048
Maintenance	40,111	43,691	40,167	35,965	24,677
Depreciation	131,611	86,210	85,125	84,935	82,735
Taxes (other than Income)	127,036	117,776	110,277	83,531	80,819
Total Oper. Rev. Deductions	2,194,130	1,590,551	1,398,786	1,292,902	1,055,279
Net Operating Revenue (Before Inc. Taxes)	519,773	331,916	382,785	430,419	361,455
Other Income	26,984	26,113	35,903	36,844	66,409
Gross Income (Before Income Taxes)	546,757	358,029	418,688	467,263	427,864
Federal and State Income Taxes	256,045	171,800	212,540#	243,948	178,813
Gross Income	290,712	186,229	206,148	223,315	249,051
Income Deductions:					
Int. on Funded Debt	29,250	30,225	31,200	32,175	33,150
Int. on Bank Notes	13,090	12,797	10,300	8,914	6,812
Misc. Int. Deductions	4,259	3,879	3,506	3,178	2,920
Amortized Debt and Capital Stock Exp.	2,153	2,153	3,926	3,926	3,896
Miscellaneous	1,806	3,545	27,205*	1,086	764
Total Income Deductions	50,559	52,599	76,137	49,279	47,542
Net Income	240,153	133,630	130,011	174,036	201,509
Preferred Dividends	25,462	26,906	28,350	30,187	28,875
Balance for Common	214,691	106,724	101,661	143,849	172,634
Times Earned:					
Int. on Funded Debt:					
Before Inc. Taxes	18.47	11.85	13.42	14.52	12.91
After Inc. Taxes	9.88	6.16	6.61	6.94	7.51
Int. on Notes & Funded Debt:					
Before Inc. Taxes	12.76	8.32	10.09	11.37	10.71
After Inc. Taxes	6.82	4.33	4.97	5.43	6.23
Total Inc. Deductions	5.93	3.54	2.71	4.53	5.24
Inc.Deds. & Pfd.Divs.	3.89	2.34	1.97	2.81	3.26
Earned Per Common Share (12,800 shs. Outstanding)	$16.77	$8.34	$7.94	$11.24	$13.49
% Operating Revenues:					
Oper. & Mtnce. Exps.	72.9%	72.1%	67.5%	65.2%	62.9%
Gross Income:					
Bef. Inc. Taxes	19.9	18.6	23.5	27.1	30.2
Aft. Inc. Taxes	10.6	9.7	11.6	13.0	17.6
Balance for Common	7.9	5.6	5.7	8.3	12.2

#Includes $52,550 as a charge in lieu of taxes due to the loss on abandonment of gas manufacturing plant.
*Includes loss on abandonment of gas plant amounting to $22,957.

Federal Power Commission, which resulted in a substantial refund in 1954, gross income and net income during the years 1951-1953 inclusive have been understated by a fairly substantial amount during this three-year period. The Company received a refund from Northern Natural Gas Company in 1954 amounting to $198,425, exclusive of interest amounting to $20,519, applicable to the years 1950-1953, and the refund after Federal income taxes and fees and bonuses amounting to $41,200 paid to officers and employees for services on the rate cases totaled $84,389, which amount was credited to earned surplus.

It is not, in our opinion, feasible to attempt to restate the earnings on the basis of the cost of gas for each of the years 1950-1953 based on the settlement of the rate case. For the three-year period 1951-1953, however, in the aggregate, net income in our opinion was understated by $84,389. Conversely, net income in 1950 was overstated by a small amount due to the deferment in the increased cost of gas in the fourth quarter of that year. The deferment of this rate increase, incidentally, was charged directly against surplus during the year 1953 in an amount equivalent to the gross amount of the cost of gas deferred ($19,271), less applicable Federal income taxes, or in a net amount of $8,664.

We are also of the opinion that net income during several of the years between 1946 and 1954 were understated because of the accounting treatment followed with respect to a number of charges. In 1946, for example, the Company included under Income Deductions $33,750 representing the premium paid on the refunding of the First Mortgage Bonds. The more normal accounting treatment, in our opinion, would have been either to have debited Unamortized Debt Discount and Expense with this item and amortize it over the life of the Bonds refunded, or to have charged the amount against earned surplus. In 1947 and 1948 Income Deductions included $7,341.62 and $9,974.02, respectively, representing an income tax deficiency applicable to prior years which again we believe might well have been charged against earned surplus. In 1952 there was included in Income Deductions a provision for loss on abandoned plant amounting to $22,957.00 which we believe might well have been charged against earned surplus. As previously mentioned, however, conversely in 1950 the increased cost of gas was not absorbed, and such increased cost of gas less applicable taxes amounting to a net figure of $8,664 was charged against earned surplus in 1953.

Other Income, which is represented largely by the net profit before Federal income taxes on merchandising and jobbing, amounted to $26,984 in 1954, a figure which compares favorably with 1953 but which is somewhat lower than 1951 and 1952, and substantially lower than 1950. While the Company continues to aggressively merchandise appliances, merchandise sales have been declining, as would be expected in view of the saturation of the market. The net profit on merchandising sales after Federal income taxes is not large in relationship to gross income.

Because of distortions in the income account due to increases in the cost of gas purchased from Northern Natural Gas Company disallowed in part, and the treatment of other accounting items, together with variations in degree day deficiencies, a comparison of the trend in gross income and net income with the trend in operating revenues is not as significant as it has been in the case of many other utility companies. Also, operating revenues increased very substantially in 1954 due to the sale of a relatively large amount of gas ($510,926) to Iowa Power & Light Company for boiler fuel. There was, however, a gradual and steady increase in operating revenues between 1946 and 1953. There was virtually no increase in gross income during the same period but there was an increase of 49% in net income. Very substantial increases in operating revenues, gross income, and net income occurred in 1954, partly as a result of rate increases which became effective on January 1, 1954 and partly as a result of sales of gas for boiler fuel to Iowa Power & Light Company.

The coverages for First Mortgage interest charges even on the basis of reported earnings have been very wide, varying from about 13 times to 18.5 times for First Mortgage Bond interest before Federal income taxes, and varying from over 6 times to nearly 10 times after Federal income taxes. The over-all coverage for Income Deductions and preferred dividend requirements has, on the whole, been quite good in spite of what we consider to be an understatement of gross income and an overstatement in two years between 1950 and 1954 of Income Deductions. The percentage of operating revenues consumed by operating and maintenance expenses has showed an increase from 62.9% in 1950 to 72.9% in 1954, but this again was due in part to the increased cost of gas included in operating expenses which the Company subsequently recovered through refunds from Northern Natural Gas Company, and in part to the sale of a relatively large amount of gas for boiler fuel on which the spread between the selling price and the cost of gas is much lower than is the case for domestic, commercial, and small industrial business.

The unusually large increase in gross income and in net income which occurred in 1954 was due in part to higher rates which were placed into effect on January 1, 1954 and in part to the relatively large sales of gas on an interruptible basis made to Iowa Power & Light Company. Although the spread between the selling price of this gas and the cost of gas purchased was not large on an M.c.f. basis, amounting to approximately 3.9¢ per M.c.f., the net profit on such business because of the volume of sales involved was important. We estimate that gross income and net income after Federal and state income taxes was approximately $33,500 in 1954 on this business, which was a fairly substantial portion of total gross and net income of the Company for that year.

Depreciation appropriations have been excellent for many years. Book depreciation has equaled that claimed for income tax purposes and in 1954 was equivalent to 3.12% of the average gross book value of depreciable property. Approximately the same rate has prevailed for many years.

Dividends paid on Common stock have varied materially by years and during the period 1950-1954 ranged from $80,000 in 1950 to $204,800 in 1954. For this five-year period in the aggregate dividends paid on Common stock amounted to $540,800, which compares with a reported balance for Common stock during the same period of $739,559, an indicated payout of 73%. Since the balance for Common stock during this period has been substantially understated, in our opinion, the relationship of Common dividends to earnings available for Common stock has been materially lower than the percentage indicated above.

Operating revenues and earnings have also been affected during the period under review by changes in degree day deficiency. The normal annual degree day deficiency is about 6,100, but in 1954 the degree day deficiency was only 5,525, or about 90.6% of normal, and was 5,545 in 1953. In 1952 the degree day deficiency was 6,204, slightly more than normal, but in 1951 the degree day deficiency was 6,976,or about 14% above normal. The degree day deficiency in 1950 was 6,622, or about 8-1/2% above normal.

Analysis of Income Account: We are giving below a breakdown of operating revenues and M.c.f. sales by customer classes in 1954:

	Revenues	%	Mcf Sales	%	Operating Revenue per Mcf
Revenues	$1,654,065	61.0	1,958,980	38.6	0.84
Commercial	261,573	9.6	396,841	7.8	0.66
Industrial	798,265	29.4	2,714,002	53.6	0.29
Total	2,713,903	100.0	5,069,823	100.0	1.79

In 1954, 29.4% of operating revenues and 53.6% of M.c.f. sales came from industrial customers, but in prior years the industrial business was very much less important. A breakdown of industrial revenues by major classifications appears at the top of the following page.

	Revenues	%	Mcf	%%	Rev. per Mcf
Iowa Power & Light	$510,926	64.0	1,856,071	68.4	27.5
Greenhouses	58,801	7.4	191,289	7.0	30.7
Union Pacific Railroad	50,387	6.3	172,887	6.4	29.1
Schools	45,281	8.9	140,271	5.2	32.3
Hospitals and Orphanages	29,099	3.6	88,274	3.3	33.0
Blue Star Produce Co.	19,305	2.4	56,766	2.1	34.0
Standard Oil Co.	6,233	.8	15,875	.6	39.3

It will be noted that 64% of industrial operating revenues were derived from sales of gas on an interruptible basis to Iowa Power & Light Company which became a customer for the first time in 1954 upon completion of its 44,000 kw. Council Bluffs steam generating plant. With the exception of the Iowa Power & Light load, none of the other industrial customers or groups contributed any large portion of operating revenues.

The Company's present residential rates which went into effect on January 1, 1954 are as follows:

First	400 cu. ft. or less	$1.25 Minimum Bill	
Next	600 cu. ft. @	.15	per 100 cu. ft.
Next	1,000 cu. ft. @	.12½	per 100 cu. ft.
Next	1,000 cu. ft. @	.10	per 100 cu. ft.
Next	7,000 cu. ft. @	.07½	per 100 cu. ft.
Next	40,000 cu. ft. @	.06	per 100 cu. ft.
Over	50,000 cu. ft. @	.05½	per 100 cu. ft.

The rate increase for residential customers was around 6.7% and followed a rate increase made late in 1952. The Company absorbed the increased cost of gas in 1950, 1951, and during most of 1952, and likewise absorbed further increases in the cost of gas during most of 1953. Because of this fact refunds obtained from Northern Natural Gas Company did not have to be passed along to customers as the rates charged to customers were not geared either through fuel adjustment clauses to the increased cost of gas, or to the increased rates charged by Northern. With respect to the general service rates, it is interesting to note that giving effect to the rate increase which became effective January 1, 1954 the cost of gas service was only about 20% more than it was in 1930 in spite of generally increased costs of doing business, including four increases in the cost of gas purchased from Northern Natural Gas.

We are giving on the following page a comparison of the cost of gas based on the present rates with those charged by a number of neighboring utilities, including the Metropolitan Utility District in Omaha.

	1950 Population	Minimum Monthly Charge	Units of Gas Used - In Therms						
			5	10	30	50	100	250	400
		$	$	$	$	$	$	$	$
Communities Served by Northern Natural Gas Co.									
Council Bluffs, Iowa	45,429	1.25	1.40	2.15	4.40	5.90	9.65	18.65	27.65
Omaha, Nebraska (Municipal)	251,117	1.00	1.09	1.54	3.34	4.99	8.74	19.99	31.24
Sioux Falls, So. Dakota	52,696	1.00	1.00	1.53	3.43	5.13	8.88	19.08	29.28
Des Moines, Iowa	177,965	0.75	0.93	1.55	3.90	5.65	8.65	17.65	26.65
Lincoln, Nebraska	98,884	1.00	1.00	1.45	3.06	4.48	7.68	16.38	25.08
Beatrice, Nebraska	11,813	1.00	1.00	1.55	3.47	5.11	8.71	18.61	28.51
Columbus, Nebraska	8,884	0.75	0.75	1.00	2.85	4.55	8.40	18.90	29.40
Mason City, Iowa	27,980	0.75	1.05	1.79	3.66	4.86	7.36	14.86	22.36
Communities Served by Other Pipelines									
Davenport, Iowa	74,549	0.75	0.87	1.60	3.79	5.73	8.40	16.41	24.42
St. Joseph, Missouri	78,588	1.00	1.00	1.00	2.11	3.22	6.00	14.32	22.64

In general, rates of the Company are somewhat higher for cooking and water heating than those which prevail for a number of other companies or systems purchasing gas from Northern Natural Gas Company, but are fairly similar for customers using gas for house heating which, in the case of the Company's territory, is an important factor since the house heating saturation is exceedingly high. Omaha, which is served by the Municipal Utilities District, placed higher rates into effect in May 1953 and again on January 1, 1955, and the rates shown in the tabulation are the present rates. Rates of Council Bluffs Gas Company are a little lower than the Omaha Municipal Utilities District rates for house heating customers and, of course, it should be remembered that the Omaha system is tax-free. Furthermore, this system requires customers to pay for service lines, whereas the Company connects directly to customers except in rural areas. The fact that rates of the Company are actually lower for house heating customers than the Omaha Municipal rates is, of course, important in view of the proximity of the two systems.

In 1954 average use per domestic customer was 152.7 M.c.f. but, as previously mentioned, the degree day deficiency in that year was about 9% lower than normal.

Special industrial rates exist for the Union Pacific Railroad and for Iowa Power & Light Company. In the case of Iowa Power & Light Company the basic rate is 5¢ per M.c.f. higher than the price paid to Northern Natural Gas. In the case of the Union Pacific the general service rate prevails for the first 100 M.c.f. used per month, and all gas consumed in excess of 100 M.c.f. is billed at 28.9¢ per M.c.f.

Operation and maintenance expenses in 1954 aggregated $1,977,574, equivalent to a little less than 73% of operating revenues. The major classification of operating expenses, exclusive of maintenance, depreciation, and taxes, was as follows:

Gas Purchased	$1,618,669
Gas Manufactured	1,592
Other Operating Expenses	316,760
Total	$1,937,021

The cost of gas is, of course, by far the largest expense item and averaged approximately 32¢ per M.c.f. Effective December 27, 1954 Northern Natural placed into effect its fifth rate increase, under bond, and the present cost of gas will be discussed under "Prospective Earnings". Northern Natural's rates which prevailed in 1954 consisted of a monthly demand charge of $2.21 per M.c.f., a basis commodity charge of 22.1¢ per M.c.f., and an "over-run" rate of 24.1¢ per M.c.f. on interruptible gas.

Operating expenses other than the cost of gas purchased and manufactured, and maintenance, totaled $316,760 in 1954 and as a matter of interest we are showing below such operating expenses by years for the period 1950-1954 and have related these to the average number of customers served:

	Amount	Average Customers	Per Customer
1954	$316,760	13,783	$23.60
1953	332,303	13,330	24.18
1952	312,602	12,868	24.30
1951	316,106	12,377	25.50
1950	302,593	11,827	25.42

Operating expenses have varied only moderately and it is interesting to note that operating expenses in dollars, in 1954, were very nearly the same as in 1951.

General and administrative expenses in 1954 amounted to $177,076, which figure was equivalent to about 56% of operating expenses exclusive of cost of gas purchased and manufactured, and maintenance, and to $12.90 per average customer served. Such administrative and general expenses, in our opinion, are rather high but reflect the payment of $20,000 to a non-resident officer of the Company and a similar amount for engineering and consultation fees. Other general and administrative expenses appear to us to be quite reasonable, and officers' salaries generally are reasonable. The president of the Company receives $15,000 annually, the operating vice president $8,400 annually, and an executive vice president $10,000 annually.

PROSPECTIVE EARNINGS

To an appreciable extent earnings of the Company during the next few years will depend upon two major situations, one, the cost of gas purchased from Northern Natural Gas Company, and the other, the amount of gas which will be sold to Iowa Power & Light Company on an interruptible basis for boiler fuel in that company's Council Bluffs generating plant. These two situations are interrelated in that the cost of gas will have a material effect on the profit margin of this business.

In December 1954 Northern Natural Gas placed new higher rates into effect under bond, representing the fifth rate increase made by this company in recent years. The new rates, which take the form of an increase in the demand charge (but not in the commodity charge) from $2.21 per M.c.f. of monthly demand to $2.70 per month of billing demand, are estimated to increase the cost of gas by $169,000 on an annual basis. Under the contract with Northern

Natural Gas Company which runs from November 1954 to October 1969, the contract demand is 21,400 M.c.f. and the contract permits an increase or decrease in contract demand.

The demand charge under the present rates, as previously mentioned, is $2.70 per month of billing demand and the commodity charge is 22.1¢ per M.c.f. The contract also provides for a credit for voluntary operation of peak shaving facilities at Northern's request, with a reduction in the demand charge should this situation occur, and there is a credit for any deficiency in the amount of gas delivered by Northern under the contract demand. The commodity rate for the overrun on interruptible gas is 24.1¢ per M.c.f. rather than the ordinary commodity charge of 22.1¢.

The Company did not pass along the increase in the cost of gas through higher rates as did the Omaha municipal system and any refunds which would be obtained if the final rates approved by the Federal Power Commission are less than the rates which have gone into effect under bond would be retained by the Company, as has been the case in the past.

It will probably be several months before the FPC hands down a decision on Northern's application for a rate increase, but it seems improbable that the full rate increase will be allowed and it is the opinion of the management of Council Bluffs Gas Company that perhaps not more than one-half of the rate increase will finally be allowed. Also the question of zone rates is before the FPC and a decision is expected within the very near future on this matter. There seems to be some reason for believing that zone rates will be approved and the Company, together with the Omaha municipal system and several other utilities, has been strongly urging zone rates. Some other companies purchasing gas from Northern have been opposing zone rates. In the event that zone rates are ordered, the probabilities are that the commodity charge would be reduced and that the demand charge may also be readjusted.

On the question of zone rates, the staff of the Federal Power Commission has recommended such a practice in the case of the Northern Natural Gas system, but the presiding trial examiner filed a decision in which he ruled that the use of uniform rates for its entire system by Northern Natural Gas should not be changed at the present time. Oral arguments were heard by the FPC on February 17 with three of Northern's customers, including Council Bluffs Gas Company, contending that customers of Northern in their area were being discriminated against by continuation of the present rolled-in rate system. The staff of the FPC also filed exceptions to the examiner's decision and supported a zone plan, although that recommended by the staff proposed different zones from that urged by Council Bluffs Gas Company. Counsel for Northern, as well as counsel for 10 of Northern's customers in the northern end of the system, argued in support of the examiner's decision.

In 1954 the Company sold a very substantial amount of gas for boiler fuel to Iowa Power & Light Company and revenues from this amounted to $510,926 on sales of 1,856,071 M.c.f. We have been informed that in 1954 the spread between the cost of gas and the price at which gas was sold to Iowa Power & Light was 3.87¢ per M.c.f. after considering the cost of overrun gas and some increase in the demand charge. Under the prevailing schedule the spread is 5¢ per M.c.f. Iowa Power & Light Company, however, has been experimenting with Oklahoma coal to determine the net cost of fuel if coal were used, and has for some time been purchasing only a relatively small amount of gas from the Company. Readjustment in the rates charged for gas appears to be a probability and it now appears as though the price which Iowa Power & Light Company can afford to pay will be around 26¢ per M.c.f. which would result in a spread, based on Northern's present rates, of about 3.9¢ per M.c.f. It is probable, however, that Iowa Power & Light will continue to burn coal for a few weeks, at least, as we understand that they have a stockpile of coal and have entered into a contract for the purchase of coal from Oklahoma mines. It is probable, therefore, that it may be 30 to 60 days before gas again is purchased by Iowa Power & Light in substantial amounts.

When we were in Council Bluffs the Company furnished us with an estimated income account based on the present Northern Natural Gas rates and on the old rates, which we are giving below:

	Present Cost of Gas	Cost of Gas Under Northern's Old Rates
Operating Revenue	$3,111,344	$3,103,844
Cost of Gas	2,069,531	1,909,806
Operation and Maintenance	390,000	390,000
Depreciation	92,821	92,821
Taxes, except Income	133,008	133,008
Total	2,685,360	2,525,635
Net Operating Revenue	425,984	578,209
Other Income - Net	24,000	24,000
Gross Income before Inc. Taxes	449,984	602,209
Income Taxes	214,709	289,815
Gross Income after Inc. Taxes	235,275	312,394
Income Deductions:		
Interest on Funded Debt	28,275	28,275
Interest on Bank Loans	10,125	10,125
Miscellaneous	4,320	4,320
Amortization of Debt Disc. & Exp.	2,153	2,153
Total Income Deductions	44,873	44,873
Net Income	190,402	267,521

Estimated net income under Northern's present rates is $190,402 for 1955 which compares with $240,153 for 1954 and $133,630 for 1953. It will be noted that had Northern's old rate prevailed, estimated net income would have amounted to $267,521. The 1955 estimate was predicated on the assumption that Iowa Power & Light would be purchasing gas for boiler fuel throughout the entire year, and included in the estimate for operating revenues was $702,500 which would net the Company $66,000 after taxes. In March, however, Iowa Power & Light purchased only a negligible amount of gas from the Company and in February purchased a considerably smaller amount of gas than had been anticipated, so that the budget includes a larger amount of operating revenues from Iowa Power & Light as well as a larger amount of net profit from this business than will be the case this year. On the other hand, the degree day deficiency during the first three months of 1955 was higher than normal and operating revenues from classes of business other than the Iowa Power & Light load were likewise higher than anticipated. In March 1955, for example, operating revenues showed an increase of $55,913 over the same month in 1954, or a 20.3% increase, although revenues derived from Iowa Power & Light amounted to only $3,456 in that month. Exclusive of the Iowa Power & Light load there was an increase of about 11% in operating revenues during the first three months of 1955 in comparison with the same period in 1954. The much colder than normal weather which prevailed during the first three months in 1955, therefore, offset to a material extent the lower than anticipated revenues from Iowa Power & Light Company.

In spite of the fact that revenues from the sale of gas to Iowa Power & Light Company were substantially less than anticipated, and in spite of the fact that the Company absorbed the higher cost of gas purchased from Northern, gross income for the first three months of 1955 amounted to $384,942 which compared with $382,066 in the same period in 1954. In March 1955 gross income amounted to $126,027 which compares with $105,355 in March 1954. The Company should enjoy a comparatively good year therefore, in 1955, as a large portion of the earnings occur during the first three months of the year.

It is our belief that under existing conditions and based on the prevailing Northern Natural Gas rates, net income in a normal weather year will probably range from $175,000 and $200,000 assuming that the Iowa Power & Light business can be retained on a fair profit margin. Earnings, we believe, would be higher than this range if Northern is not granted the full increase in rates applied for, which appears to be a reasonable expectation.

Net income of approximately $200,000 would be equivalent to gross income of around $245,000. Such a figure is equivalent to about 10% of the carrying value of utility plant less reserve for depreciation and contributions for construction. However, the rates of the Company are lower than the Omaha system rates for most house heating customers in spite of the fact that that system is tax-exempt, and the Company did not pass along the higher cost of gas following the rate increase by Northern even though the Omaha system did. The Company appears to have handled its rate negotiations with the city on a very constructive basis, and as long as this continues we would anticipate that the Company could earn a relatively high return on its investment in property.

From a longer-term standpoint there is the possibility that the cost of gas may increase further. Northern Natural Gas apparently desires to purchase gas from Canada and estimates which have been made by the Company indicate that net income in 1955 on the basis of the cost of Canadian gas, and with no zoning of the Northern system, would reduce net income to around $134,000. The Company as well as most gas distribution systems purchasing from Northern are vigorously opposing arrangements under which Northern would purchase Canadian gas, and the proposed Canadian pipeline has not been financed.

It is impossible, of course, to predict what earnings of the Company would be if Northern were to obtain a substantial amount of gas from Canada and were allowed to pass along the increased cost of gas to its customers. It would not seem unreasonable to believe, however, that even if the cost of gas purchased from Northern should increase the Company could pass along a substantial portion of the higher cost of gas, particularly if the Omaha municipal system did so. If the cost of interruptible gas should increase substantially, however, the Iowa Power & Light business, which is important, might be lost or the profit margin on such business might be reduced to a lower amount than that which prevailed in 1954 or is expected to prevail in 1955.

The territory served by the Company is not growing rapidly and the growth in customers is now running at the rate of about 400 to 500 annually, so that no unusually large increase in revenues other than interruptible sales is anticipated, particularly since the saturation for house heating is very high. There is a possibility, however, that Iowa Power & Light Company will enlarge its Council Bluffs plant possibly by 1958 or 1959, although we do not believe that any final decision has been made on this question. If the Council Bluffs steam plant is enlarged it is anticipated that the second unit would be 66,000 kw., which compares with 44,000 kw. for the first unit, and this development would greatly increase the amount of interruptible sales and have an appreciable effect on net income assuming that Council Bluffs Gas can continue to sell gas on a fair profit margin.

FINANCIAL POSITION AND REQUIREMENTS

As of March 31, 1955 current and accrued assets totaled $758,043, of which cash amounted to $377,729. As of the same date current and accrued liabilities, including $79,596 of customers' deposits, totaled $774,439, and an indicated working capital deficit of $16,396 existed. There was, however, a substantial decrease in the working capital deficit between the end of 1954 and March 31, 1955, as would be expected since earnings are comparatively large during the first three months of each fiscal year.

During the period 1950-1954 gross additions varied from $125,066 in 1954 to $223,264 in 1952, and averaged about $156,400 during this period. Gross construction expenditures in 1952, however, were substantially higher than normal.

The Company estimates that construction requirements will amount to $125,000 in 1955, $100,000 in 1956, and $75,000 in 1957, which are relatively small for a company of this size. Depreciation appropriations now amount to approximately $93,000 and are nearly as large as the average anticipated annual construction requirements during the next three years. However, the Company's sinking fund payments, including the repayment of Notes Payable in the amount of $60,000 annually, are quite substantial amounting to $121,500 annually, and such sinking fund requirements would, in effect, have to be met from additional financing except to the extent that earnings were retained.

It is anticipated that the Company will make a $60,000 payment on the Notes Payable to banks on May 15, but will borrow an additional $60,000 under the Note Agreement either prior to or after May 15.

We are of the opinion that the present capital structure of the Company is not a suitable one and that a substantial reduction in sinking fund requirements can be accomplished through refunding of the existing First Mortgage Bonds, Sinking Fund Preferred Stock, and Notes Payable. Were this done only a relatively small amount of additional capital would be required during the next few years, assuming that a reasonable amount of net earnings available for Common stock were retained.

MANAGEMENT, PUBLIC RELATIONS, AND REGULATION

In our opinion, the operating management of the Company is experienced and understands the problems of operating a gas distribution system such as this which obtains its gas supply from a large pipeline company whose rates are regulated by a Federal administrative body, and which rates therefore are not under control of the Company itself. While there has been a rather wide fluctuation during recent years in reported gross income and net income, we believe that reported earnings have been understated throughout the period. However, the Company has earned an excellent return on the average on the investment in property, and on Common stock equity. The fact that Northern Natural Gas Company made four rate increases during the period under review, plus a fifth rate increase which went into effect late in 1954 but which had no appreciable effect on 1954 earnings, created a difficult managerial situation as well as problems with respect to public relations.

The general policy which seems to have been followed by the Company was one of passing along only that portion of the increased cost of gas which the management estimated would finally be allowed by the FPC. Since no state regulatory body having jurisdiction over the rates of the Company exists in Iowa, negotiations for rate increases have had to be made on the city level. We read with interest the letter of the Company to the Mayor of the city dated November 13, 1954 when the last rate increase was requested, which seemed to us to explain the situation very well and which was followed by prompt approval of the City Council. It was, of course, exceedingly helpful that the near-by Omaha municipal system likewise increased rates on several occasions, including one effective January 1, 1955, which was not followed by a request for higher rates on the part of Council Bluffs Gas Company. So far as we have been able to ascertain, relations between the Company and the city have been amicable and public relations also appear to be good.

The principal operating officials are still relatively young and have been with the Company for many years. The president of the Company had been with Lone Star Gas and remained with the Council Bluffs Gas property after control of the Company was sold by Lone Star Gas.

In our opinion, good control over such operating expenses as have been under the control of the local management has been exercised and the management for many years has aggressively merchandised appliances. With the saturation of the market, however, the number of new appliances sold has declined during the past two or three years. In 1953 the Company sold a total of 842 appliances, including 255 ranges, 242 water heaters, 69 refrigerators, and 38 floor furnaces. In 1954, 164 ranges, 164 water heaters, 22 refrigerators, and 41 floor furnaces were sold, and in 1954 the total number of appliances sold was 581. The Company estimates that it sells between 30% and 40% of the ranges sold in its territory, about 50% of the water heaters, and about 95% of the conversion burners.

It is estimated that about 50% of the water heating sales are now for replacement and most of the conversion burners likewise are for replacement, as a very high saturation exists in the house heating load.

The management of the Company has aggressively protected the Company's interests in rate proceedings before the Federal Power Commission involving Northern Natural Gas Company, and has intervened in the cases now before the Commission. The management also has been closely following the experiments which Iowa Power & Light Company has been making covering the use of coal rather than gas and is, in our opinion, thoroughly cognizant of the importance of retaining this business on a fair profit margin.

The employees of the Company are not unionized.

In 1952 the Company obtained a new 20-year franchise which was approved by a large majority of the voters. This franchise provides for compensation to the city of $7,500 annually, plus 1% of gross receipts derived from general service rates within the corporate limits of the city, and also permits the Company to charge customers for service lines, which is the practice in Omaha, but the Company has not availed itself of this right except in rural areas.

ALB:AR
April 26, 1955

That part of the following described alleys lying South of the center lines of Lots 3 and 11, Block 12, extended and joined, to-wit:

The alley lying between the West line of Lots 1 to 6 inclusive and the East line of Lots 7 and 8, and the alley lying between the East line of Lots 9 to 14 inclusive, and the West line of Lots 7 and 8, all in Block 12, Riddle's Subdivision of the City of Council Bluffs, Pottawattamie County, Iowa,

nd the Mayor and City Clerk of the City of Council Bluffs be and they are hereby authorized nd directed to execute and deliver to said Company, its successors or assigns, a quit claim eed conveying the portions of the alleys granted above.

Section 3. The following described portions of the alleys vacated above are ereby granted to the Union Pacific Railroad Company, its successors or assigns, to-wit:

Those portions of the alleys described below lying North of a line 146 feet North of the South line of Block 11, and parallel thereto, to-wit:

The alley lying between the South line of Lots 17, 18, 19, and 20, and the North line of Lots 7, 8, 9, and 10, and the alley lying between the East line of Lots 11 to 16 inclusive, and the West line of Lots 17 and 10 extended and joined, and the alley between the east line of Lot 20 extended southward 20 feet and the West line of Lots 1, 2 and 3, all in Block 11, Riddle's Subdivision of the City of Council Bluffs, Pottawattamie County, Iowa, and,

That portion of the alley between the West line of Lots 1 to 6 inclusive and the East line of Lots 7 and 20 extended and joined, lying between the south line of Lot 20 extended east and the north line of Lot 7 extended east, all in Block 11, Riddle's Subdivision of the City of Council Bluffs, Pottawattamie County, Iowa, and,

That portion of the alleys described below, lying North of the center lines of Lots 3 and 11 in Block 12, extended and joined, to-wit:

The alley lying between the West line of Lots 1 to 6 inclusive and the East line of Lots 7 and 8, and the alley lying between the East line of Lots 9 to 14 inclusive, and the West line of Lots 7 and 8, all in Block 12, Riddle's Subdivision of the City of Council Bluffs, Pottawattamie County, Iowa,

hereby authorize

NG CERTAIN ALLEYS IN BLOCKS 11 AND 12 OF RIDDLE'S SUBDIVISION
, IOWA, AND CONVEYING PORTIONS THEREOF TO THE CITIZENS GAS
CESSORS OR ASSIGNS, AND PORTIONS THEREOF TO THE UNION PACIFIC
ORS OR ASSIGNS, AND AUTHORIZING THE EXECUTION OF QUIT CLAIM
NCE AND DIRECTING THE PUBLICATION OF THIS ORDINANCE IN THE
HE EXPENSE OF THE GRANTEES AND THE CERTIFICATION OF THIS
RDER OF POTTAWATTAMIE COUNTY, IOWA, AT THE EXPENSE OF THE

n made to appear to the City Council of the City of Council
and Electric Company of the City of Council Bluffs and its
ure and distribution of gas for illuminating and heating
ncil Bluffs have for many years, to-wit: since September 7,
lowing described property, to-wit:

, 9, 10, 11, 12, 13 and the South 10 feet
in Block 11, and Lots 4, 5, 6, 7, 12, 13,
e South Half of Lots 3 and 11 and the South
of Lot 8 in Block 12 in Riddle's Subdivision
ity of Council Bluffs, Pottawattamie County,

time the said Company and its predecessors as above described
alleys within and adjoining the Lots hereinbefore described,
ecifically described below; and,

been made to appear to said City Council that the Union Pacific
many years held title to the following described property, to-wit

, 2, 3, 15, 16, 17, 18, 19, 20, and Lot 14,
the South 10 feet thereof, in Block 11, and
1, 2, 9, 10, and the North Half of Lots 3 and
nd Lot 8, except the South 22 feet thereof, in
12, Riddle's Subdivision of the City of Council
s, Pottawattamie County, Iowa,

time said Railroad Company and its predecessors have used and
n and adjoining the Lots hereinabove described, such alleys being
bed below; and,

e opinion of the City Council of the City of Council Bluffs there
rdinance authorizing the vacation of such alleys and granting the
but the same has not been preserved of record, and the record there
but said Companies have for many years paid taxes on such vacated
erty.

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Lots 7
East line
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Subdivision
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be and they are hereby authori
ccessors or assigns, a quit cl

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North of
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Lots 17,
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Pottawattamie

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Lots
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To: Council Bluffs MGP File   September 3, 1991

From: Dan Schroeder - Engineering

RE: 8/30/91 Ground Water Level

I requested Geotechnical Services to read the groundwater elevations at the Council Bluffs, IA MGP site in order to obtain updated groundwater elevations to assist in the preparation of the phase II proposal/work plan. The measurements were taken on August 30, 1991.

WELL #	MEASUREMENT *
MW-1	15.51
MW-2	19.25
MW-3	17.05
MW-4	15.99

* Measurements taken from the north edge of the riser pipe.